

# **Water Quality and Drinking Water Revolving Loan Fund Programs**

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## **I. PURPOSE**

The purpose of this Program Manual is to provide potential Borrowers with an overview of the Maryland Water Quality and Drinking Water Revolving Loan Fund Programs and to help ensure compliance with Federal and State regulations and other Program policies. Organizationally, the Maryland Water Quality Financing Administration (MWQFA or Administration) is responsible for managing the financial and legal requirements of the State Revolving Loan Fund (SRF) while the Water Management Administration (WMA) is responsible for managing the technical and eligibility requirements. Both Administrations are within the Maryland Department of the Environment (MDE or Department).

## **II. OVERVIEW**

### **A. Maryland Water Quality Revolving Loan Fund (WQRLF or WQSRF)**

Consistent with the Federal Clean Water Act of 1987, the WQSRF was established in 1988 pursuant to the Maryland Water Quality Administration Act, Title 9, Subtitle 16 of the Environmental Article, Annotated Code of Maryland. The purpose of the WQSRF is to make low interest rate loans to local governments and eligible private entities for water quality infrastructure projects, while establishing a perpetual source of revolving funds.

The Maryland WQSRF may provide loans for the following types of water quality projects:

1. Construction of publicly-owned wastewater treatment works, as defined in Section 212 of the Federal Clean Water Act, which are identified on the State's Project Priority List. Examples include:
  - New Wastewater Treatment Plants and Upgrades and Expansions of Existing Facilities including Biological Nutrient Removal (BNR)
  - Extension and Rehabilitation of Sewage Collection and Conveyance Systems including Pumping Stations
  - Sewage Sludge Handling Facilities and Equipment
  - Backwash Facilities at Drinking Water Treatment Plants
  - Publicly Owned Industrial Pretreatment Facilities including

## Landfill Leachate Treatment

2. Implementation of nonpoint source pollution controls under Section 319 and estuary conservation and management plan under Section 320 of the Federal Clean Water Act. Examples include (also see [Appendix K](#)):

- Capping of Existing Landfills
- Stormwater Control Best Management Practices
- Stream Restoration/Stream Bank Stabilization
- Wetlands Creation/Restoration
- Agricultural Best Management Practices
- Septic System Repair/Restoration
- Replacement of Leaking Underground Storage Tanks

### **B. Maryland Drinking Water Revolving Loan Fund (DWRLF or DWSRF)**

In anticipation of amendments to the Federal Safe Drinking Water Act (SDWA) of 1996, the DWSRF was established in 1993 pursuant to amendments to the Maryland Water Quality Administration Act, Title 9, Subtitle 16 of the Environmental Article, Annotated Code of Maryland. The purpose of the DWSRF is to make low interest rate loans to both public and privately-owned community water systems and non-profit non-community water systems for drinking water infrastructure projects, while establishing a perpetual source of revolving funds.

The Maryland DWSRF may provide loans for the following types of projects:

- Existing Drinking Water System Upgrades
- Finished Water Storage Facilities
- Consolidation of Smaller Water Systems
- New Drinking Water Facilities to Correct Public Health Problems

### **C. Funding Sources**

The funding for both the WQSRF and the DWSRF is provided through annual Federal appropriations that require a 20% State fund match. The MWQFA is authorized to issue revenue bonds by pledging the loan principal and interest repayments to pay debt service on bonds. The excess repayments and investment earnings are part of the respective SRFs and are also available to make additional loans.

### **III. SRF LOAN INTEREST RATES, TERMS AND FEES**

#### **A. Interest Rates**

The interest rate on SRF loans is set as a percentage of "market rate" to provide an interest rate subsidy to the Borrowers. The MWQFA market rate is defined as the average of the Bond Buyer 11-Bond Index (BB11-BI) for the month preceding the loan closing. The interest rates for loans from the two SRF Programs are as follows:

Water Quality SRF Program	40% of Market Rate/BB11-BI
Drinking Water SRF Program	40% of Market Rate/BB11-BI (Could be lower for a Disadvantaged Community*)

#### **B. Term of Loan**

Water Quality SRF Program	Up to 20 years
Drinking Water SRF Program	Up to 20 years (up to 30 years for a Disadvantaged Community*)
* See <a href="#">Appendix A</a> for States definition of Disadvantaged Community - WQSRF (A-1) and DWSRF (A-2).	

#### **C. Loan Origination Fee**

None.

#### **D. Administrative Fee**

There is an Administrative Fee equal to 5% of the aggregate debt service divided by the number of administrative fee payments over the life of the loan (generally equal to loan term). This fee is collected annually and is used for Program operating expenses. This fee amounts to approximately 0.50% (50 basis points)

increase in the loan interest rate.

The above loan interest rates, terms and fees are applicable to loans financed through the Department and not applicable to loans financed through the Linked Deposit Program (see Section IV-B below).

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## **IV. LOAN PROCESS**

The following is a brief summary of the SRF Loan Process:

- Pre-application submitted to MDE (any time) or during annual solicitation during January through February of each year
- Project reviewed for consistency with Maryland's Smart Growth Legislation and rated/ranked based on approved priority systems (WQSRF or DWSRF)
- Based on priority ranking and readiness to proceed, project is included on the annual Intended Use Plans for WQSRF or DWSRF.
- Public Hearing on the Intended Use Plan and subsequent approval by the United States Environmental Protection Agency (USEPA)
- Financial Analysis/Credit Review undertaken by MWQFA (all loans except through Linked Deposit)
- Engineering/Environmental Review (if applicable) undertaken by WMA
- Project approved for Loan Execution (Direct or Linked Deposit)

### **A. Direct Loan from the MWQFA**

Eligible Borrowers may seek a direct loan from the MWQFA. This would involve completion of a final loan application, securing legal representation, and execution of a loan agreement typically backed by a general obligation pledge (public entities) or by other means of security (private entities). The MWQFA may pledge certain tax-exempt loans to a future revenue bond issue. The Borrower must also comply with the following key program requirements:

- MDE approval of the final Design Plans and Specifications
- Competitive bidding on construction contract with a Minority/Women Business Enterprise (M/WBE) participation goal of 14% of the loan amount for projects funded by federal capitalization grant/state match funds. MDE will provide the borrower with the % M/WBE goal applicable

to their project. (also see section V-J and [Appendix G](#))

- MDE approval of procurement prior to loan payment reimbursement

## **B. Loan via the Linked Deposit Program**

The MWQFA amended its enabling legislation in the 1998 session of the Maryland General Assembly to allow both the WQSRF and the DWSRF Programs to provide loans to borrowers through certain local banks via a Linked Deposit Program.

An eligible Borrower may seek a loan through the Linked Deposit Program. The Linked Deposit Program is a mechanism that can provide below market rate of interest loans through a network of private lending institutions. For example, a landowner with an approved Best Management Practice (BMP) may apply to one of the network of banks for financing at a below market rate of interest. The lender (Bank) will evaluate the creditworthiness of the applicant, and if the lender determines the borrower's credit is acceptable, will apply to the Administration for an investment agreement equal to the loan amount and term. The investment agreement will be at a below market rate of interest that will be passed on by the lender to the Borrower. The below market rate of interest investment agreement is "Linked" to the below market rate of interest loan. The loan agreement is between the lender and the Borrower, and as such the lender assumes all risk of default, and may charge origination and other reasonable fees associated with the loan.

For nonpoint source pollution control or estuary conservation and management plan projects under the WQSRF, a Borrower may start the process printing the Linked Deposit Certification of Qualification Form from the MWQFA web-site or by requesting it from MDE or their local approving authority. The nonpoint source pollution control or estuary conservation and management plan projects eligible under WQSRF are approved on a first come first served basis and do not undergo a priority rating or ranking. The Department, when preparing its annual Intended Use Plan will identify the amount of funds being allocated for WQSRF projects using the Linked Deposit Program.

For drinking water projects under the DWSRF, the borrower must apply directly to the Department so that the project is rated and ranked. Once the project is selected for DWSRF financial assistance, the borrower may use the Linked Deposit Program to secure loan funding through a lending institute, similar to nonpoint source pollution control projects under the WQSRF as indicated above.

For additional information regarding the Linked Deposit Program, the borrower should contact MDE at (410) 631-3574 or (410) 631-3119.

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## **V. GENERAL SRF PROGRAM INFORMATION AND REQUIREMENTS**

The following requirements are applicable to most Water Quality and Drinking Water SRF Loan projects financed directly through the MWQFA, and are generally not applicable to projects considering financing through the Linked Deposit Program, except as noted below:

### **A. Project Priority List and Intended Use Plan**

Pre-applications ([Appendix B](#)) for potential SRF loan projects are accepted at any time during the year. In addition, the Department solicits pre-applications through a mailing to local governments and eligible private community water system owners each January. Projects are rated/ranked based on the approved priority systems for Water Quality ([Appendix L](#)) or Drinking Water ([Appendix M](#)) projects. The priority system is used to assign points based on the project's water quality and public health benefits, and to establish two separate (WQSRF and DWSRF) Project Priority Lists (PPLs). Projects are selected from the PPLs and identified for financial assistance on the respective WQSRF or DWSRF Intended Use Plans (IUPs). The proposed projects must also meet the threshold requirement for consistency with the Maryland Smart Growth and Neighborhood Conservation (Smart Growth) legislation. The draft PPLs and draft IUPs are mailed to all local governments and eligible private community water system owners, and are subject to a public hearing prior to adoption. The final IUP is submitted to the USEPA annually to request Federal grant funds, which provide the seed money for the SRF Programs to make low interest rate loans. In addition to a list of projects identified for financial assistance, the IUPs provide an update on the current status of the SRF Programs. New projects may be amended into the PPL and the IUP during the year, and delayed projects identified on the IUPs may be bypassed or deleted based on the Project Bypass Policy ([Appendix C](#)).

The above requirement is applicable to all projects (MWQFA Direct loan or Linked Deposit loan) except for certain privately-owned nonpoint source pollution control or estuary conservation and management plan projects under WQSRF, considering financing using the Linked Deposit Program. Based on the availability/allotment of funds for WQSRF Linked Deposit projects, the projects



will be approved on a first come first served basis and will not undergo priority rating or ranking. The Department, when preparing its annual Intended Use Plan will identify the amount of funds being allocated for WQSRF Linked Deposit Program.

**B. Refinancing (Not applicable to Linked Deposit Program)**

The MWQFA may refinance local debt obligations of public entities to reduce the interest rate and/or to extend the loan maturity date for an eligible project, provided certain debt conditions and program requirements are met. The Borrower should also seek the advice of bond counsel and/or tax attorney to ensure that such refinancings are consistent with the IRS provisions under the Tax Reform Act of 1986. Contact MWQFA for specific project refinancing eligibility.

**C. "Official Intent" – Internal Revenue Service Regulations (Not applicable to Linked Deposit Program projects)**

On June 18, 1993, the Treasury Department revised reimbursement regulations affecting the use of bond proceeds to reimburse expenditures paid by an issuer prior to the issuance of the Bonds. These regulations affect public sector Borrowers who intend to reimburse project expenditures from tax-exempt bond proceeds including a loan from the MWQFA. These regulations are effective for debt issued after June 30, 1993 and require compliance with the procedures detailed in the regulations for declaring "official intent" prior to making any expenditures that are to be reimbursed with proceeds of tax-exempt debt (with a limited exception for certain preliminary expenditures). Accordingly, Borrowers should take official intent to reimburse prior to incurring project costs (other than planning and design) in strict compliance with IRS regulations.

**D. Credit Analysis (Not applicable to Linked Deposit Program projects)**

For all loans through the Department, the MWQFA reviews the financial condition of the enterprise fund (e.g., water/sewer fund, solid waste fund etc.), as well as the overall fiscal health of the Borrower. The past and projected financial performance of the Borrower is a key part of the analysis in making the determination to approve a loan. The primary concern is to ensure that the designated revenues are sufficient to support adequate operations and maintenance, and the existing and proposed debt. Where revenues are inadequate, the Administration will work with the Borrower in preparing a fiscal plan to

support the loan. Based on the analysis, the borrower may be required to increase user rates and/or establish a debt service reserve account. If the financial analysis indicates that the loan would result in excessive user charges, the Administration will work with the Borrower to secure other means of financial assistance, where possible, to reduce the impact of the loan (also see [Appendix A - Disadvantaged Community Criteria](#)).

**E. Double Barreled Pledges (Not applicable to Linked Deposit Program projects)**

For loans made by MWQFA to local governments, the Administration will require both a Revenue Pledge (e.g., water and/or sewerage enterprise fund) and a General Obligation (GO) Pledge, where the Borrower pledges its full faith and credit to the repayment of the debt. In some cases, the MWQFA may accept only a Revenue Pledge, where the Borrower pledges to repay the loan solely from the revenues from a specified source such as the revenues from the enterprise fund. In such cases, where a GO Pledge of the taxing power of the Borrower or parent entity is not possible, additional loan conditions shall mandate additional credit enhancements in lieu of the GO pledge. Revenue pledges are accepted only if the loan has a senior lien (first claim) on the revenue of the Enterprise Fund after payment of reasonable operating and maintenance expenses. For a revenue pledge to be acceptable, a user charge system must demonstrate that the existing or projected level of revenue is sufficient to pay for operations and maintenance costs, and debt service on the proposed loan. In addition, the Loan Agreement may include a rate covenant and an additional debt service coverage test. The MWQFA will negotiate the terms of these covenants with the Borrower on a case by case basis.

**F. State-Aid Intercept (Not applicable to Linked Deposit Program projects)**

As an additional measure of security, all local government Borrowers must agree, as a condition of the loan, to permit the State Comptroller to pay the MWQFA from State Aid normally due to the Borrower, in the event of a debt payment default.

**G. Declination of a Loan**

The MWQFA will not make a loan if the Administration determines the loan amount would place an undue burden on the financial resources of the Borrower. If the potential Borrower cannot demonstrate adequate financial capacity, the Department will assist the Borrower in meeting Water Quality and Drinking

Water project needs by seeking other forms of financial and technical assistance. For projects considering financing through the Linked Deposit Program, the lending institution will determine whether to make the loan or not, based on the borrower's creditworthiness.

## **H. Engineering Report and Environmental Review**

The borrower should submit an engineering report/planning document outlining the following:

- Proposed Project Scope/Estimated Cost
- Water Quality/Public Health Benefits/Issues
- Public Participation/Community Support
- Environmental Impacts/Permits Necessary

Prior to providing loan assistance, the WMA will perform an environmental review of the proposed project in compliance with the State Environmental Review Procedures (SERP) outlined under COMAR 26.03.11 ([Appendix D](#)). The environmental review requirement applies to all Drinking Water and Wastewater projects (MWQFA loan or Linked Deposit), and is not applicable to Nonpoint Source Pollution Control projects or Estuary Conservation and Management projects eligible under Sections 319 and 320 of the Federal Clean Water Act.

Borrowers may submit environmental information for the project by completing the Preliminary Environmental Screening Checklist (Addendix E). Based on the type and complexity of the project, the WMA Project Manager will advise the Borrower to complete an Environmental Information Document ([Appendix F](#)) or to prepare an Environmental Impact Statement, if necessary. As part of the SERP, the WMA will summarize its preliminary environmental assessment and issue a notice in the project area for public comments. The WMA will also provide the Maryland Office of Planning (MOP) project information to undertake an inter-agency State Clearinghouse Review. After addressing any public and MOP comments, the WMA will take its final action under the SERP.

## **I. Project Consistency with Maryland's Smart Growth Legislation**

All proposed projects must be consistent with the Maryland Economic Growth, Resource Protection and Planning Policy under Executive Order 01.01.1992.27 and with the Priority Funding Areas under the 1998 Maryland Smart Growth legislation. The Project Priority Ranking Systems use consistency with "Smart

Growth" as a threshold requirement. The WMA will inform the Borrower if the project is inconsistent with "Smart Growth" and how a project may qualify for an exception in case of overriding public health concerns.

**J. Project Design Plans and Specification Approval (Not applicable to Linked Deposit Program projects)**

At least 30 days prior to advertising for bids, the Borrower should submit for approval to WMA the final Plans and Specifications and if applicable, the Application for Water and Sewerage Construction Permit.

One key Program requirement is the Minority/Women Business Enterprise (M/WBE) participation goal of 14% of the loan amount for projects using federal capitalization grant and state match funds. The Department will provide the Borrower with an "SRF Insert" - Requirements and Contract Provisions for the Project Financed through the Maryland Water Quality and Drinking Water Revolving Loan Fund ([Appendix G](#)), indicating the M/WBE percentage goal specific to the project. The Borrower is required to include this SRF Insert in the contract specifications for the bidders to comply with certain Federal/State Program requirements. To accomplish the M/WBE goal, the Borrower and Contractor must demonstrate (as part of MDE's procurement review and approval process – see below) that the following affirmative steps were undertaken:

1. Including small, minority, and women's businesses on solicitation lists;
2. Assuring that small, minority and women's businesses are solicited whenever they are potential sources;
3. Dividing total requirements, when economically feasible, into small tasks or quantities to permit maximum participation by small, minority and women's businesses;
4. Establishing delivery schedules, when the requirements of the work permit, which will encourage participation of small, minority and women's businesses;
5. Using the services of the Small Business Administration and the Office of Minority Business Enterprise of the U.S. Department of Commerce, as appropriate.

**K. Procurement Approval (Not applicable to Linked Deposit Program projects)**

The Borrower must obtain prior written approval from the WMA before awarding any construction contract. The borrower should submit to WMA, at least 30 days prior to bid expiration, items identified in the procurement approval package

([Appendix H](#)). The key elements of the procurement package include: updated project budget, evidence of advertisement, bid tabulation, selected bidder's cost proposal, certain assurances, and information regarding Minority and Women Business Enterprise participation.

**L. Final Loan Application (Not applicable to Linked Deposit Program projects)**

The Borrower must complete a Final Loan Application ([Appendix I](#)) generally, after opening construction bids and at least 60 days prior to loan closing. The Final Loan Application includes information on project cost and requested loan financing, project/loan disbursement schedule, economic and financial data, and a list of key local officials/contacts. The Loan Officer will assist the Borrower in completing the Final Loan Application.

**M. Loan Closing Documents (Not applicable to Linked Deposit Program projects)**

The Administration will close the loan with the Borrower and will deliver closing documents and a final debt service schedule. In exchange, the Borrower will deliver to the Administration its Loan Obligation, which is defined as a bond, note, or other evidence of obligation issued by the Borrower to evidence its indebtedness under the Loan Agreement. Along with the Loan Obligation, the Borrower will deliver an opinion of tax counsel, acceptable to the Administration that states that the Loan Obligation is tax-exempt (if applicable), within the definition of the Internal Revenue Code. The Loan Officer will assist the Borrower through the process.

**N. Request for Loan Disbursements (Not applicable to Linked Deposit Program projects)**

The SRF loan fund disbursements are made on an "Incurred Cost" basis or on a "Reimbursable Cost" basis. For example, the borrower may choose to request disbursement of loan funds concurrently with vendor billing or may choose to pay its vendor and then request loan disbursement. The borrower is required to submit supporting project cost invoices along with a Cash Draw Request Form ([Appendix J](#)) when seeking loan reimbursement. Loan disbursements WILL NOT be made until the WMA has authorized the procurement/contract award and has received a copy of the signed construction contract (or A/E agreement, purchase order, etc.), and where applicable, the notice-to-proceed, performance and payment bonds, and proof of adequate liability insurance. For disbursement of borrower's "administrative costs", the Cash Draw request must include

supporting documentation identifying costs associated with the project specific cost center. For projects being financed through the Linked Deposit Program, the lending institution will determine the loan disbursement procedures.

**O. Construction Inspection and Monitoring**

The Borrower will provide sufficient competent inspection and engineering supervision at the construction site to ensure that the construction work conforms to the approved plans and specifications. The Borrower will permit the WMA staff to visit the construction site during normal working hours to monitor project progress and to attend progress meetings. For projects being financed through the Linked Deposit Program, the Department or its designee may periodically monitor the project construction, in addition to any construction monitoring requirements by the lending institution.

**P. Interest During Construction (Not applicable to Linked Deposit Program projects)**

The interest accrued during construction is calculated on the amount of funds drawn by the Borrower (similar to a line of credit) and repaid on February 1, and August 1, each year, while the project is under construction.

**Q. Project Closeout (Not applicable to Linked Deposit Program projects)**

Upon completion of the Project Final Inspection, the WMA will forward to the Borrower a Final Disbursement Package to request its final loan disbursement and facilitate project closeout.

**R. Loan Repayments**

Repayment of principal must begin within one year after completion of construction or one year following the date of estimated construction completion as specified in the Loan Agreement. Loan repayments for a projects refinanced through the SRF must begin within one year following disbursement. Working within these guidelines, the first loan repayments can be negotiated to best fit the Borrower's needs. For "public" borrowers, the MWQFA collects the principal plus interest on February 1, and the interest plus administrative fee on August 1, each year. For "private" borrowers, the MWQFA collects the principal, interest and administrative fee quarterly on February 1, May 1, August 1 and November 1, each year. The MWQFA will bill each Borrower a month before the loan repayment is due. For projects being financed through the Linked Deposit

Program, the lending institution will determine the loan repayment schedule.

**S. Loan Prepayment**

Loans may be prepaid with the permission of the MWQFA Director.

Prepayments are permitted where the Borrower makes the Administration whole for any losses or costs associated with the prepayment. For projects being financed through the Linked Deposit Program, the lending institution will determine the loan prepayment procedures.

**T. Disclosure and Due Diligence (Not applicable to Linked Deposit Program projects)**

All public sector Borrowers will be required to provide the Administration with annual audited financial statements. Private sector Borrowers, in lieu of audited financial statements, may provide income tax returns, public service commission financial reports, etc. The Administration may also request additional information, as needed, to make a full disclosure of all pertinent information.